

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of
ODD FELLOWS TEMPLE ASSOCIATION OF PASADENA

Appearances:

For Appellant: George Herbert Wood, Certified Public
Accountant
For Respondent: Chas. J. McColgan, Franchise Tax Commission

O P I N I O N

This is an appeal pursuant to Section 25 of the Bank and Corporation Franchise Tax Act (Chapter 13, Statutes of 1929, as amended) from the action of the Franchise Tax Commissioner in overruling the protest of Odd Fellows Temple Association of Pasadena to a proposed assessment of an additional tax in the amount of \$77.83, based upon its return for the year ended December 31, 1933.

In January, 1932, Appellant caused an audit of its records to be made which disclosed that its treasurer had embezzled sums totalling \$3,892 from Appellant during the years 1930 and 1931. The treasurer admitted the defalcations and gave to Appellant a promissory note payable in ninety days for the amount embezzled. Following her failure to make payment in accordance with the note, criminal proceedings were instituted against her which resulted in a six months jail sentence. Upon her release from jail, she obtained housework, but her earnings were insufficient to permit her to make payments on the note. In 1933; she apparently left the state, her whereabouts became unknown, and in October, 1933, the note was charged off on Appellant's books as a debt ascertained to be worthless.

In its return for the year ended December 31, 1933, Appellant made a deduction from gross income on account of the debt. The Commissioner disallowed the deduction on the grounds that it was applicable to a prior year and proposed the additional assessment in question.

The general rule seems to be that losses from embezzlement can be deducted only in the year in which the embezzlement occurs. (See Klein, Federal Income Taxation, Par. 18:35) Notwithstanding this rule, we held in the Appeal of The First National Bank in Glendale (decided by this Board on June 3, 1933) that losses due to embezzlement could be deducted under Section 8(e) of the Act as a debt ascertained to be worthless in the year in which it is ascertained that the person committing the embezzlement is unable to make restitution of the amount embezzled. In the course of our opinion, we expressed ourselves as follows:

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"We think it proper to observe that if losses resulting from embezzlement could be deducted only in the year in which the embezzlement occurred, taxpayers would often be denied any deduction of such losses. Where embezzlements occur over a number of years, it may be difficult or impossible to ascertain the exact amount embezzled in any particular year or years. Furthermore, it may well happen, as in the instant case, that the embezzlements will not be discovered until it is too late to claim a deduction for the loss resulting therefrom if the deduction must be taken in the year of the **embezzlement.**"

In view of this decision, it is clear that Appellant was not confined, in taking a deduction for the loss in question, to the years 1930 and 1931, when the embezzlement occurred. It does not follow, however, that Appellant was entitled to take a deduction in the year 1933.

As noted above, Appellant discovered the embezzlement in the early part of 1932. It does not appear that the treasurer committing the embezzlement had assets or prospects of making repayment sufficient to justify Appellant in concluding with any degree of certainty that, **notwithstanding** the embezzlement, it had not in fact sustained a loss, but would eventually recover the amounts embezzled.

It may be argued that if Appellant had not reasonably **ex-**pected to obtain recovery, it would not have accepted a note from the treasurer but would have had criminal proceedings instituted against her immediately. This argument loses **whateve**r force it may have when it is considered that the treasurer failed to make payments in accordance with her note, and, following her failure, criminal proceedings were instituted against her,

In our opinion, it was not necessary for the treasurer to disappear in 1933 to cause one to believe that there was but little likelihood of obtaining so large a sum as \$3,892 from her. The fact that she did not make payment on her note, particularly in view of the circumstances under which the note was apparently given, plus her conviction and sentence to jail, plus the fact that upon her release, she was forced to do housework, were sufficient.

Since all of these facts were known to Appellant in 1932, we think the Commissioner's conclusion that the debt was ascertained worthless in 1932 can scarcely be considered unreasonable

O R D E R

Pursuant to the views expressed in the opinion of the Board **on file** in this proceeding, and good cause appearing therefor,

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IT IS HEREBY ORDERED, ADJUDGED AND DECREED, that the action of Charles J. McColgan, Franchise Tax Commissioner, in overruling the protest of Odd Fellows Temple Association of Pasadena, a corporation, against a proposed assessment of an additional tax in the amount of \$77.83, based upon the return of said corporation for the year ended December 31, 1933, pursuant to Chapter 13, Statutes of 1929, as amended, be and the same is hereby sustained.

Done at Sacramento, California, this 25th day of October, 1935, by the State Board of Equalization.

R. E. Collins, Chairman
John C. Corbett, Member
Fred E. Stewart, Member
Orfa Jean Shontz, Member
Ray L. Riley, Member

ATTEST: Dixwell L. Pierce, Secretary